



January 28, 2016

Ex Parte Notice

Ms. Marlene H. Dortch, Secretary
Federal Communications Commission
445 12th Street, S.W.
Washington, D.C. 20554

Connect America Fund, WC Docket No. 10-90; A National Broadband Plan for Our Future, GN Docket No. 09-51; Establishing Just and Reasonable Rates for Local Exchange Carriers, WC Docket No. 07-135; High-Cost Universal Service Support, WC Docket No. 05-337; Developing a Unified Intercarrier Compensation Regime, CC Docket 01-92; Federal-State Joint Board on Universal Service, CC Docket No. 96-45; Lifeline and Link-Up, WC Docket No. 03-109

Dear Ms. Dortch:

On Thursday, January 26, 2016, the undersigned, on behalf of Vantage Point Solutions (VPS) had a telephone call with Joseph Sorresso of the Wireline Competition Bureau. During the call, as part of a broader effort to test and finalize various aspects of potential universal service reform, the method used by the Capital Budget Mechanism (CBM) to calculate the Total Allowed Loop Expenditure (TALE) was discussed.

The CBM starts from the respective gross plant investments of Rate of Return Local Exchange Carriers (RLECs) to estimate the investment needed to construct networks in the future in their study areas. The gross plant investment from the RLEC's financials are adjusted by an inflation factor to "bring forward" the gross plant investment into today's dollars. Within the CBM, this adjusted gross plant investment is referred to as the TALE and it sets an upper limit on the investments that can be recovered by the RLEC through universal service support.

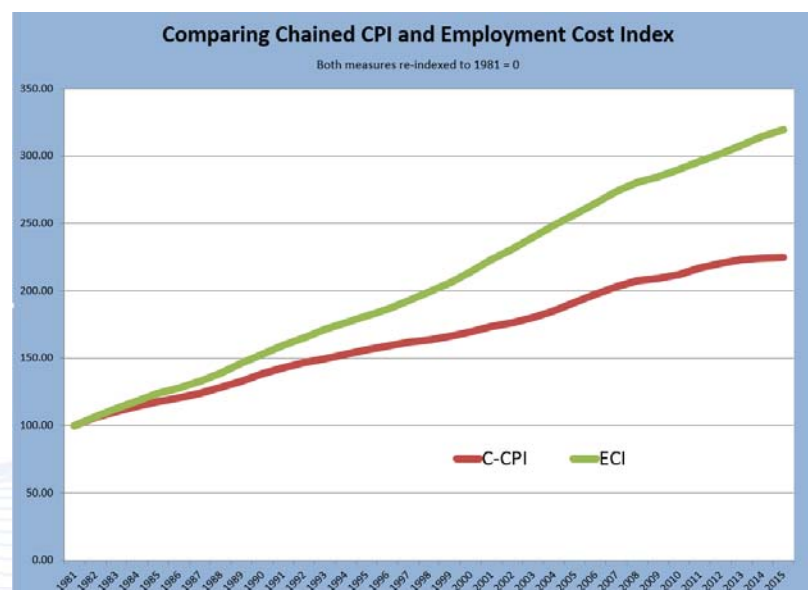
In order for the TALE to accurately estimate the cost to construct a network within a given study area, it is necessary for the inflation index to be similar to and highly correlated with inflation of the historical costs associated with outside plant (OSP) construction of networks generally. Since all other calculations in the CBM depend upon the TALE, if the TALE is in error, then the Annual Allowed Loop Expenditure (AALE) – the "annual budgets" for recoverable capital expenditures – will also be in error. In particular, if the index consistently underestimates the OSP construction inflation, it will hurt those with older cable plant the most, since the error introduced will be compounded over a number of years.

One way to test the accuracy of the CBM's method for calculating the TALE would be to compare the TALE for a RLEC to the cost to construct a network throughout its entire study area (either engineering estimates or actual construction costs). However, most companies only engineer

individual exchanges when they are ready to construct and do not normally engineer all of the exchanges in their study area in advance.

Over the last 10 years, VPS has engineered more than \$1.5B of outside plant construction and manages 5,000-10,000 miles of construction per year. It has been our experience that approximately 70% of OSP construction costs in RLEC areas are associated with labor. Because of this, we feel it would be important to use an inflation index that is similarly weighted on labor inflation. Errors in the choice of the inflation index may not be critical in instances where the plant is not very old, since the difference between the adjusted and unadjusted gross plant investment would be small. However, the CBM could artificially and arbitrarily limit the investment of companies with older plant if the inflation index underestimates the actual inflation, since the error in the index would be compounded over a large number of years.

The Chain-Weighted Consumer Price (C-CPI-U) index, which has been discussed previously for possible use in the CBM, tracks inflation with respect to the cost of goods and services such as food, clothes, housing, transportation, and medical care. Although there is a labor component to the C-CPI-U, it is much less than the percentage of labor associated with OSP construction. By contrast, the Employment Cost Index (ECI) is a widely-utilized measure of labor inflation. As can be seen in the chart below, the C-CPI-U materially understates the impact of inflation over time relative to the ECI. The ECI or another labor-heavy index (or blending of indexes) more closely tracks the true inflation related to outside plant construction and is therefore a more realistic and reasonable means of “bringing forward” older network construction costs to reflect today’s costs of construction. We therefore strongly urge the FCC to utilize the ECI or another index more reflective of growth over time in labor costs as part of the CBM or any comparable efforts to set forward-looking capital investment budgets. Goals with respect to network deployment in rural areas, and in unserved areas in particular where network upgrades are needed to achieve certain levels of broadband access, will be frustrated if an inaccurate inflationary index is utilized.



In addition, because of the unique areas served by the RLECs, the FCC should make available a simplified, streamlined waiver process for instances where the inflationary index used still does not provide a TALE that is adequate to provide broadband to all (or most) of the customers in their study area. Absent such a waiver, efforts (or requirements) to reach certain unserved areas may prove futile, if not impossible, over time. Even with an inflation index that is closely correlated with OSP construction inflation, there may still be a number of reasons why a given company's gross plant adjusted for inflation may not be representative of the actual cost to construct a broadband-capable network in its study area. This is primarily due to local factors that would increase the cost of construction and might have emerged since that company's last major construction, such as:

- A national forest or national park has been established in the service area
- Additional underground utilities (rural water, gas and oil lines, etc.)
- Increased environmental and historical regulations and requirements
- Increased state or local cable depth requirements
- An aging pole infrastructure that may require replacement

Therefore, in instances where a RLEC can show that the TALE (*i.e.*, its historic network levels of investment "brought forward" to current costs via an inflationary index) does not accurately represent the cost to replace very old depreciated plant and construct a new network in its study area, that RLEC should be able to seek and obtain a waiver process on a relatively streamlined basis to ensure that it is able to make the investments necessary to provide broadband to its customers in spite of factors that are likely outside of the RLEC's control. One means of establishing such a streamlined process could be to require the RLEC to have a professional engineer that is licensed in the relevant state to provide a detailed engineering estimate of the costs associated with constructing to a network in the study area. This engineer could account for all local construction factors when determining the estimate. The Rural Utilities Service has successfully relied on a similar process for many years.

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Pursuant to Section 1.1206 of the Commission's rules, a copy of this letter is being filed via ECFS with your office. If you have any questions, please do not hesitate to contact me at (605) 995-1777 or Larry.Thompson@Vantagepnt.com.

Sincerely,

/s/ Larry D. Thompson

Larry D. Thompson
Chief Executive Officer
Vantage Point Solutions

cc:
Joseph Sorresso